B-177648

COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

December 14, 1973

Spitz & Grossman
Twenty-First Floor
The 600 Building
Corpus Christi, Texas 78401

Attention: Oscar Spitz, Esquire

Gentlemen:

Reference is made to your August 13, 1973, letter to this Office requesting reconsideration of our decision, B-177648, August 10, 1973, relative to the claim of Centron Corporation (Centron) for royalty payments in connection with Value Engineering Change Proposal (VECP) EG-01, submitted by Elegant Garments, Incorporated (Elegant), under contract No. DAAA09-69-F-0046, between the Small Business Administration (SBA) and the United States Army Ammunition Procurement and Supply Agency (APSA). You believe reconsideration is warranted because of a factual error in the decision.

This contract, entered into on September 4, 1968, pursuant to section 8 (a)(1) of the Small Business Act, 15 U.S.C. 637 (a)(1), called for the furnishing of 310,000 bandoleers for 40mm cartridges at a price of $201,500. On September 13, 1968, SBA entered into subcontract No. SBA-0022-8(a) with Elegant pursuant to section 8 (a)(2) of the Small Business Act, 15 U.S.C. 637 (a)(2), for the performance of the prime contract.

SBA and APSA, on August 19, 1969, entered into Contract No. DAAA09-70-C-0006 for an additional quantity of 200,000 bandoleers for an additional amount of $130,000. This additional quantity was added to the original subcontract between SBA and Elegant by Modification No. 1 to that subcontract, raising the total contract price to $331,500.

Centron and Elegant entered into an agreement on September 24, 1969, whereby Elegant obtained all of Centron's rights, title and interest in VECP EG-01. This VECP suggested that a cost saving could be realized if uncapped snap fasteners were substituted for the capped fasteners specified by the Government. Pursuant to this agreement Elegant submitted the VECP for the Government's consideration, whereupon the Government agreed to pay Elegant royalties for the VECP in accordance with the pertinent provisions in Elegant's SBA contract.

The agreement between Elegant and Centron also provided that Elegant would pay Centron 65 percent of all monies realized under ...

[Claim for Royalty Payments]

the VECP. Subsequently court action was initiated by Centron to enforce its agreement with Elegant, and ultimately a judgment order was entered whereby a joint escrow account was established with a bank as escrow agent for receipt of royalties, which was in accordance with the parties' original agreement. SBA acknowledged receipt of a notice of assignment of royalties to the bank in October 1970. On December 1, 1970, and March 11, 1971, SBA paid into the joint escrow account the sums of $9,078.56 and $69,485.97, respectively, less certain deductions due SBA by Elegant.

In a transaction not related to any of the above matters or contracts, the Small Business Administration Regional Director, Midwestern Regional Office, Chicago, Illinois, on August 28, 1969, approved a direct loan by SBA to Elegant in the amount of $40,000 pursuant to section 7(a) of the Small Business Act. Elegant executed a promissory note in the amount of $40,000 dated October 31, 1969. In a letter to this Office dated February 28, 1973, SBA stated that since Elegant has defaulted in the payment of this loan, it is SBA's intention "to set off any future royalty payment due Elegant and received by SBA under its contracts with APSA against Elegant's indebtedness." As of September 13, 1973, SBA has received the sum of $23,356.85 as royalty payments due Elegant under contracts Nos. DAAA09-69-F-0046 and DAAA09-70-C-0006 and subcontract No. SBA-0022-8(a).

We have reconsidered our prior decision and, although we note a mistake as to the facts in that opinion, we affirm its final determination. In that opinion we referred to the $40,000 given by SBA to Elegant on August 28, 1969, as an advance payment under its subcontract with SBA. As noted above, this was incorrect. The $40,000 constituted a loan from SBA to Elegant. However, characterizing the payment as a loan does not alter our earlier determination.

The Government's right to withhold payment in this case stems from its common law right of set-off. While Elegant's debt to the Government arose from a transaction unrelated to the bandoleer contracts, nevertheless the Government has the same right of set-off "which belongs to every creditor, to apply the unappropriated moneys of his debtor, in his hands, in extinguishment of the debts due to him." United States v. Munsey Trust Co., 332 U.S. 234 (1947); McKnight v. United States, 98 U.S. 179 (1878); and Gratiot v. United States, 40 U.S. 336 (1841).

You originally argued that the arrangement between Centron and Elegant was "a joint venture to secure and perform a public contract." While the Government may not use contract monies to extinguish the unrelated debt of one of a contractor's joint venturers (Economy Plumbing & Heating Co., Inc. v. United States, 456 F.2d 713 (Ct. Cl. 1972)) we do not find a sufficient basis for concluding that such privity of contract existed between the Government and Centron under the bandoleer contracts. Inasmuch as Centron assigned its rights, title and interest in the VECP to Elegant and since the royalties became due upon performance of the contract by Elegant and Centron's participation only encompassed a small aspect of the performance by Elegant, we cannot conclude that Centron is entitled to payment as a joint venturer.

As to the Government's right of set-off against the assignee-bank, in the absence of an effective no set-off provision in the contract the Government is entitled to set-off against an assignee-bank any of its claims against the assignor-contractor which had matured prior to the assignment. South Side Bank & Trust Company v. United States, 221 F. 2d 813 (1955); 37 Comp. Gen. 318, 320 (1957); and B-170494, August 12, 1970. The record before us indicates that the SBA loan became due on August 31, 1970, whereas receipt of notice of the assignment was acknowledged in October 1970. (Assignments are effective only after notification. 31 U.S.C. 203.)

In any event, the bank appears to be acting here merely as an escrow agent for ultimate distribution to its principals, Centron and Elegant, and has no financial interest in the contractor's operations under the contract. In such circumstances we would regard the assignment, in practical effect, as having been made to the principals, Centron and Elegant. B-171552, April 27, 1971. Since assignments of accounts receivable from the United States can be lawfully made only to financing institutions within the meaning of the Assignment of Claims Act of 1940, 31 U.S.C. 203, and since the bank's principals do not meet this criteria, we do not regard such an assignment to the agent bank as enforceable against the Government. 49 Comp. Gen. 44, 46 (1969) and cases cited therein.

Accordingly, we remain of the opinion that the Government's set-off action was proper.

Sincerely yours,

Paul G. Dembling

For the Comptroller General
of the United States